October 26, 2009
To: Interested Parties
From: Phillip Oliff, Center on Budget and Policy Priorities (oliff@cbpp.org)
Re: Food Tax Relief Options for Utah

Utah has several options for offsetting the impact of an increase in the state's sales tax on food for low-income families. Any mechanism for this purpose should meet three criteria. First, it should be relatively easy and inexpensive to administer. Second, it should be scalable so that it can be set at a level that is reasonably likely to offset the impact of the sales tax on food on low- and moderate-income families. (An average family in the bottom quintile of the income distribution spends $2,369 per year on food[1], meaning that a 4.75 percent food tax would cost it $113.) Third, it should be structured in a way that maximizes the number of families that can (and do) claim the credit.

This memo discusses two options in light of those criteria:

- An Earned Income Tax Credit
- A food tax credit modeled on credits from other states

Each of these options has its advantages.

**Earned Income Tax Credit:** An EITC would offset the increase in the food tax for working-poor and near-poor families, particularly families with children. The credit would be extremely easy to administer, requiring just one additional line on the Utah tax form and one calculation (multiplying the federal credit that a family receives by a set percentage rate). Of those that are eligible for the EITC, experience at the federal level, and in other states shows that take-up rates are very high — in the range of 80-85 percent — meaning that most households who qualify actually receive the credit. (Some 156,071 Utah families claimed the credit in 2007.)

A potential drawback of the EITC as a means of food tax relief is that it excludes those low-income households that have no wage income, mostly elderly and disabled families and individuals. Additionally, the EITC pays minimal amounts to low-income workers with no children.

**Food Tax Credits:** A majority of the states that apply their full sales taxes to food for home consumption provide targeted tax credits to offset the impact of the food tax for low income families (see appendix for descriptions); Utah could adopt a similar credit. These credits tend to follow a common simple structure and are generally administered through the income tax, which makes them almost as simple to administer as the EITC. (A separate, simple application can be provided for people who otherwise would not be required to file income taxes, a group that includes most low-income seniors and people with disabilities.) Such credits typically provide a modest rebate to all households with incomes below a specified level. The size of the refund varies according to family size (and sometimes according to income). The advantage to using this kind of credit to offset the increase in the sales tax on food is that it can be designed so that all households are eligible for the credit. An open question, however, is whether most families would claim the credit; although data are scant, there is reason to believe that take-up rates among those not otherwise required to file tax returns would be low (perhaps as low as 50

[1] According to the Bureau of Labor Statistics' Consumer Expenditure Survey

percent). A low take-up rate would reduce the fiscal impact of a credit, but make it much less effective in achieving its goal of offsetting the food tax increase.

A Utah food tax credit should probably be approximately $65 per person to entirely offset the full 4.75 percent sales tax on food, or $40 per person to offset the proposed three percent increase in the food tax.[2] The credit amount could phase down at higher income levels to avoid having the credit suddenly fall to zero after income passes a certain threshold.

**A combined approach**

As described above, the EITC has higher participation rates. The food tax credit is available to a wider range of families. If a goal is to offset the grocery tax for the full range of low-income families who otherwise would be made worse off, a good solution would be a combination of the two approaches. Other states do this; for example both Kansas and Oklahoma provide both a food tax credit and a refundable EITC. Offering both credits rather than just one is not complicated, since neither credit on its own is very complex. (Some working-poor families with children would be eligible for both credits; in such a case, the additional credit would serve to offset other taxes those families pay, such as sales taxes on other goods.)

## Appendix: Food Tax Credits in Other States

| State | Amount of Credit/Rebate | Eligibility Requirements | Cost and Number of Claimants |
|---|---|---|---|
| Hawaii | Ranges from $10 to $85 per exemption and varies by income with lower income households receiving larger credits. | Available to all households with adjusted gross income below $50,000. | Cost: $7.5 million (in 2005)<br><br>Number of families claiming credit: 174,638 (in 2005) |
| Idaho | $30 per exemption for households with taxable income above $1000 or $50 per exemption for households with taxable income of $1000 or less. The elderly receive an additional $20. (Credit amounts are for 2008).<br><br>Scheduled to increase by $10 per year until the credit reaches $100. | Available to all households. | Cost: $82.8 million (estimated for 2010)<br><br>Number of claimants: Unavailable |
| Kansas | $50 per exemption if qualifying income is $15, 151 or above, $80 per exemption if qualifying income is below $15, 151. | Available to families with children, the elderly, and disabled with qualifying household income less than $30,300. | Cost: $35.9 million (in 2007)<br><br>Number of Families Claiming Credit: 285,000 (in 2007) |
| Oklahoma | $40 per exemption | Available to families with children with gross incomes | Cost: $37.8 million (in 2005) |

[2] These figures are calculated using data from the Bureau of Labor Statistics' Consumer Expenditure Survey. The calculation takes per-person food expenditures at home for the bottom income quintile, and multiplies that number by the applicable food tax rate.

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| | below $50,000, and individuals and married couples with no dependents with gross incomes below $20,000. | Number of beneficiaries: Approximately 945,000 (in 2005) |